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In the Supreme Court of the United States

OCTOBER TERM, 1958

No. 409

ESTATE OF JOHN IVERSON, MARDRID REITE DAVISON, ET AL., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The findings of fact and opinion of the Tax Court (R. 132–145) are reported at 27 T. C. 786. The opinion of the court of appeals (Pet. 17–29) is reported at 255 F. 2d 1. The supplemental opinion of the court of appeals denying petitioners' motion to recall the mandate (Pet. 53–55) is reported at 257 F. 2d 408.

JURISDICTION

The judgments of the court of appeals were entered on May 9, 1958 (Pet. 30–33). By order of Mr. Justice Burton dated July 17, 1958, the time to petition for a writ of certiorari was extended to October 6, 1958. The petition for a writ of certiorari was filed

on September 29, 1958. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254 (1).

QUESTION PRESENTED

Whether, for purposes of the five-year statute of limitations applicable when gross income omitted from the return exceeds 25% of the "gross income" reported (§ 275 (c), Internal Revenue Code of 1939), "gross income" from sales means gross receipts or gross receipts less cost of goods sold.

STATUTES AND REGULATION INVOLVED

Internal Revenue Code of 1939 (26 U. S. C., 1952 ed.):

> SEC. 22. GROSS INCOME.
>
> (a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * *, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *
>
> * * * * *
>
> SEC. 275. PERIOD OF LIMITATION UPON ASSESSMENT AND COLLECTION.
>
> Except as provided in section 276—
>
> (a) *General Rule.*—The amount of income taxes imposed by this chapter shall be assessed

within three years after the return was filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period.

* * * * *

(c) *Omission from Gross Income.*—If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 5 years after the return was filed.

Treasury Regulations 111:

SEC. 29.22 (a)–5. *Gross Income From Business.*—In the case of a manufacturing, merchandising, or mining business, "gross income" means the total sales, less the cost of goods sold, plus any income from investments and from incidental or outside operations or sources. * * *

STATEMENT

Taxpayers (or their decedents) owned, in varying proportions, four partnerships engaged in the wholesale and retail selling of electrical supplies and fixtures. In the partnership returns for 1947 and 1948, taxpayers reported only sales for which cash had been received during the year and did not report credit sales for which payment had not been received (Pet. 18–19; R. 136). They included in the cost of goods sold and other deductions, however, the costs and expenses relating to all items actually sold during the

year, whether for cash or on credit (Pet. 28). A proportionate part of each item reported on the partnership returns was then reflected in each partner's individual return.[1]

The Commissioner, in notices of deficiencies directed to each partner, held that the credit sales were required to be reported in the year of sale (Pet. 18). Both the Tax Court and the court of appeals upheld that determination and it is not questioned here (Pet. 20–24). The deficiency notices were issued on January 30, 1953, more than three but less than five years after the taxpayers had filed their returns for 1947 and 1948 (Pet. 18–19; R. 140). The omitted credit sales amounted to less than 25% of the total sales reported by the partnerships but to considerably more than 25% of the gross profit (sales less cost of goods sold) reported (R. 135–136). Each partner's share of the omitted sales also exceeded 25% of his share of the gross profit plus other income reported by him (Pet. 28; R. 139). Since the cost of all sales had been deducted on the original returns, the inclusion of the omitted sales directly increased both gross profit and net income by the full amount of those sales (Pet. 28).

The Tax Court held that since the omissions from the returns exceeded 25% of the reported "gross in-

[1] The individual returns showed only each partner's share of the partnership "net income" (R. 138). For purposes of decision, however, the Tax Court accepted petitioners' argument that, for purposes of determining "gross income" under § 275 (c), the individual returns should be read together with the partnership returns, with a proportionate share of each item in the partnership return being attributed to each partner (R. 141–142).

come" the five-year statute of limitations provided in § 275 (c) of the Internal Revenue Code of 1939 was applicable and hence that the deficiency notices were timely (R. 140–144). The court of appeals affirmed (Pet. 17–29) and denied petitioners' motion to recall the mandate and for leave to file a petition for rehearing (Pet. 53–55).

ARGUMENT

Petitioners make the novel argument that "gross income", as used in § 275 (c), means not gross profit from sales (sales less cost of goods sold) but rather gross receipts, and hence that the omitted gross income[2] should be compared only with the reported gross receipts in applying the 25% limitation. Although the 1954 Code did adopt such a definition of "gross income" for purposes of the statute of limitations (§ 6501 (e) (1) (A)), the 1939 Code contained no such special definition and thus the generic meaning of the term was controlling. The universally-accepted accounting meaning of the term was accordingly adopted in the regulations, and "gross income" from sales was defined as "total sales, less the cost of goods sold."[3] Treas. Regs. 111, § 29.22 (a)–5. That definition has never, to our knowledge, been ques-

[2] The omitted sales constituted omitted "gross income" under any definition of that term, since all the costs relating to them had already been claimed on the returns.

[3] The general definition of "gross income" in § 22 (a) of the 1939 Code would also seem to require this construction. That section defines "gross income" as including "gains, profits, and income" derived from "sales," which would seem to require reduction of sales proceeds by the cost of the goods sold in arriving at gross income.

tioned and has been applied without exception by both the Tax Court (*e. g., Rose* v. *Commissioner,* 24 T. C. 755) and the courts of appeals (*e. g., Carew* v. *Commissioner,* 215 F. 2d 58 (C. A. 6)). Petitioners cite no authority to the contrary.

Petitioners' sole reliance is upon *Colony, Inc.* v. *Commissioner,* 357 U. S. 28. There the taxpayer had accurately reported in his return the proceeds from a sale of lots but had overstated his cost "basis" for the lots, with a consequent reduction in the gain—*i. e.,* gross income—shown on the return. There was no dispute over the meaning of "gross income" and it was assumed by all parties, and the Court, that only the gain (amount realized less the basis) constituted gross income. The sole question was whether an overstatement of basis, with a consequent *reduction* of gross income, constituted an *omission* from gross income of "an amount properly includible therein." The Court held that § 275 (c) was intended to apply only to a failure to report in the return an item which should have been reported and not to an overstatement of basis or of deductions. In short, the decision was an interpretation of "omits" and not of "gross income" and, to the extent that it is relevant at all, supports the definition of "gross income" applied below.

CONCLUSION

The decision below is clearly correct and in no way conflicts with this Court's decision in *Colony, Inc.* v.

Commissioner. No other conflict is alleged. The petition for a writ of certiorari should be denied.

Respectfully submitted.

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